

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. (This is a GIL.)

February 8, 1999

Dear Ms. Xxxxx:

This letter is in response to your letter dated December 16, 1998. The nature of your letter and the information you have provided require that we respond with a General Information Letter which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

I am writing to your office at the suggestion of the Peoria auditors' office. I am requesting a letter ruling on the question of receiving reimbursement from our customer for supplies we purchase on their behalf.

COMPANY is a service company that provides support services to the automotive industry, mainly paint booth cleaning and management services. Our customer in Illinois is BUSINESS. As a courtesy to our customer, we purchase and maintain an inventory of the supplies used in the performance of our service. When we purchase these supplies (our vendors charge us IL use tax), BUSINESS reimburses us for these supplies plus a 5% management fee to perform this service for them. When COMPANY was audited, we were informed by your auditors that we were supposed to treat BUSINESS's reimbursement to us for the supplies as a retail sale and charge them a 1% retail sales tax in addition to the state use tax.

Since COMPANY does not sell supplies to BUSINESS for profit, we were not aware that their reimbursement to us should have been considered a retail sale. If BUSINESS had purchased these supplies themselves, as many of our customers in other states do, they would've paid IL use tax. We therefore assumed that when we purchased the supplies, we were only liable to pay use tax on the supplies and then receive reimbursement from BUSINESS.

As a result of the audit, we have changed the way we bill BUSINESS for the supplies. We now charge them a lump sum amount (billed bi-weekly in equal increments) to cover the supplies we use. We continue to pay use tax to our vendors when we purchase the supplies. The Illinois auditors have informed us that the lump sum we bill for the supplies is not subject to retail sales tax since we no longer bill for the supplies on an item for item basis. Their interpretation was that since we are not receiving direct reimbursement from BUSINESS for the supplies, and we are billing them for a pre-determined amount and not on an 'as used' basis, these lump sum amounts are not subject to the retailers'/service occupation tax.

The auditors suggested I write your office and explain these circumstances so that we may obtain a letter ruling on this matter. I understand the purpose of a letter ruling is to verify that what the Illinois auditors told us is correct, and to keep in our files for clarification purposes during any future audits. I look forward to hearing from you, and if you have any questions or need further explanations, please call me at #####. I have attached samples of our billing to our customer. Thank you in advance for your cooperation.

We are not familiar with the facts of the audit that you mention in your letter. Therefore, the following is information of a general nature on the topics you mentioned.

Persons who provide cleaning services and use cleaning supplies as part of those services incur Use Tax liability on the cost price of those cleaning supplies. In Illinois, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See the enclosed copy of 86 Ill. Adm. Code 150.101. If the purchases occur in Illinois, the purchasers must pay the Use Tax to the retailer at the time of purchase. If the purchases occur outside Illinois, purchasers must self assess their Use Tax liability and remit it directly to the Department. The State Use Tax rate is 6.25%. A credit is given for the amount of tax properly due and paid to another State on the purchase of those cleaning supplies. See, 86 Ill. Adm. Code 150.310.

The recipients of the cleaning services incur no tax liability in regards to the use of the supplies by the cleaning service providers. This is true even if the cleaning service providers charge the recipients a fee for the cleaning supplies that the cleaning service providers use in providing those services. The cleaning supplies are being used by the cleaning service providers, not the recipient of the services. The cleaning supplies are being used by the cleaning service providers and may not be purchased for resale by the cleaning service providers.

Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. For your general information we are enclosing a copy of 86 Ill. Adm. Code 140.101 regarding sales of service and Service Occupation Tax.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred.

If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See, 86 Ill. Adm. Code 140.101(f) enclosed. This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self-assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers, nor are they liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis.

I hope this information is helpful. The Department of Revenue maintains a Web site which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.